In the Supreme Court of the United States

OCTOBER TERM, 1966

No. 428

SECURITIES AND EXCHANGE COMMISSION, PETITIONER

v.

UNITED BENEFIT LIFE INSURANCE COMPANY

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

REPLY BRIEF FOR THE SECURITIES AND EXCHANGE COMMISSION

In its brief in opposition respondent points out (pp. 4-5, 16) that, in holding in *VALIC* [1] that the variable annuity there involved was a "security" and not "insurance," this Court stressed that the company had assumed none of the investment risks, since it gave the annuitant no guarantee of any fixed income; and it argues that since it, unlike the company in *VALIC*,

[1] *Securities and Exchange Commission* v. *Variable Annuity Life Insurance Co.*, 359 U.S. 65.

does assume some investment risk by virtue of its guarantee—a guarantee, however, upon which the court of appeals recognized there was no "substantial possibility" that the company would ever be liable (Pet. 21)—its "Flexible Fund Annuity" is an insurance contract.

The argument is a *non sequitur*. For the fact that a variable annuity in which the company assumes no investment risk is not an insurance contract does not prove the converse, namely, that a variable annuity in which the company does assume some investment risk is an insurance contract.

This Court has warned that "words of our opinions are to be read in the light of the facts of the case under discussion. * * * General expressions transposed to other facts are often misleading" (*Armour & Co.* v. *Wantock*, 323 U.S. 126, 133). The decision in *VALIC* rested on the narrow ground that, since "the concept of 'insurance' involves some investment risk-taking on the part of the company," an arrangement which "places all the investment risks on the annuitant, none on the company" (359 U.S. at 71) was not insurance. In view of that limited ruling, there was no occasion for the Court to reach, and it therefore did not decide, the converse of that proposition, which this case presents: Whether respondent's "Flexible Fund Annuity" is an insurance contract solely because the company assumes some investment risk. That question cannot be answered, as respondent would do, solely by reference to the language of the *VALIC* opinion. Rather, it involves the basic policy consideration that a purchaser of respondent's "Flex-

ible Fund Annuity" has the same need for the protections Congress provided for investors in the Securities Act of 1933 and the Investment Company Act of 1940 as the purchaser of the variable annuity involved in *VALIC*, and for the same reason: that he basically is being sold a participation in a pool of equity securities that he anticipates will increase in value. See the petition, pages 8-9.

Indeed, it is difficult to believe that Mr. Justice Brennan would have joined in the Court's opinion in *VALIC* (359 U.S. at 73) if that decision determined that the federal securities laws are inapplicable to the type of variable annuity here involved. For, as our petition demonstrates, the rationale of his concurring opinion (in which Mr. Justice Stewart joined) compels the conclusion that respondent's variable annuity is not an insurance contract exempt from the coverage of the federal securities laws.[2]

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[2] The flaw in respondent's reasoning is further shown by its attempt to analogize its flexible fund contract to a traditional participating annuity (Br. in opp., pp. 20-21), which concededly is an insurance contract under the federal securities laws. In a participating annuity, a portion of the annual premium may be returned to the purchaser as a "dividend." To be sure, the amount of such "dividend" may depend upon the success of the company's business during the preceding year. But such success primarily relates to the company's insurance operations—its mortality experience, operating expenses, etc.—and not, as in the present case, to increases in the value of its securities portfolio. Since the bulk of an insurance company's assets traditionally are invested in debt securities, the amount of the participating "dividends" reflects the success of the company's investment program largely in the sense that such "dividends" will be higher if the interest rate on such debt securities is higher than anticipated—and such

In short, *VALIC* did not decide the important question presented in this case—a question which, as shown in our petition, this Court should decide.

Respectfully submitted.

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higher interest rates may well result not from the success of the company's investment program but from a change in interest rates generally. See Mehr and Osler, *Modern Life Insurance* (3d ed. 1961), pp. 570-571; Huebner and Black, *Life Insurance* (6th ed. 1964), pp. 294-300, 313-322, 387-390, 392; Maclean, *Life Insurance* (9th ed. 1962), pp. 61, 91-92, 142, 144-145, 154, 169-170, 350-351. See also the May 1965 issue of "The Tally of Life Insurance Statistics," a monthly publication of the Institute of Life Insurance, which reports that as of March 31, 1965, only 2.63 percent of the investments held by all United States life insurance companies consisted of common stocks. Moreover, to whatever extent the dividends may reflect the company's investment experience, once declared they are the property of the insured, and unlike the payments under respondent's "Flexible Fund Annuity," their amount does not depend upon the future market performance of the company's securities portfolio.

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